



Local Programs Procedures

LPP 99-01 Interim Preaward Audits Requirements

Reference: *Local Assistance Procedures Manual*, Chapters 3, “Project Authorization,” and 10, “Consultant Selection”

Effective Date: April 1, 1999

Approved: _____

HUGH G. BRADY
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Design and Local Programs

Preaward audits are required for all engineering and design related service contracts, greater than \$75,000, financed with State or Federal-aid highway funds. This LPP allows Caltrans or the local agency to perform the required preaward audit. This LPP also clarifies when an audit is not required.

There are still a number of issues regarding these requirements that will be addressed by a small work group that has been set up. The work group includes representatives from Caltrans, the Federal Highway Administration, and cities and counties; the group will look for ways to streamline and simplify the requirements. This LPP is issued on an interim basis for use until the work group recommendations are completed.

EXISTING PROCEDURES

Issuance of LPP 98-02 was based on Title 23 of the Code of Federal Regulations (CFR), part 172, section 5 (23 CFR 172.5), and on approval from the FHWA Division Administrator. LPP 98-02 made each local agency responsible for performing their own preaward audit without Caltrans’ involvement. The local agencies have the authority to waive a preaward audit, but the LPP did not provide any specific guidance to implement the waiver. Several agencies have expressed concerns as to when an audit waiver applies, and about allowing Caltrans to continue performing the audit. These and other concerns are addressed in this revised LPP.

NEW PROCEDURES

The local agencies now have the option of requesting Caltrans to perform the preaward audit rather than doing it themselves. A better explanation of when an audit is not required (waived) is

Caltrans - Office of Local Programs
April 1, 1999

also provided. In the *Local Assistance Procedures Manual*, Exhibits 3-A, 10-A (reinstated February 1, 1998 version), and 10-J (modified 10-A in LPP 98-02) reflect these changes. These changes are incorporated in the following revised procedures:

PREAWARD AUDIT

At the discretion of the local agency, either Caltrans or the local agency shall perform (or contract to perform) the required preaward audit of a consultant contract when State or Federal-aid highway funds participate in the contract.

Consultant contracts costing \$75,000 or less are exempt from the preaward audit requirements.

PREAWARD AUDIT REQUIRED

On consultant (and subconsultant) contracts more than \$75,000, a preaward audit shall be required if one of the following applies:

- There is inadequate knowledge about the consultant's accounting procedures.
- There has been a previous, unfavorable experience with the consultant's estimating or accounting methods.
- The audit has been requested by the local agency, consultant, or Caltrans.
- It is the first time the consultant has performed services for any local, State (including Caltrans) or Federal agency.
- The consultant contract is in excess of \$250,000.
- An audit has not been performed within the last 12 months.

PREAWARD AUDIT NOT REQUIRED

On consultant (and subconsultant) contracts less than \$250,000, a preaward audit is not required if a preaward audit was conducted on the consultant within the last 12 months by any local, State (including Caltrans) or Federal agency and the following are satisfied:

- A. If a preaward audit was conducted by a State or Federal agency
 - Previous preaward audit report is obtained
 - Cited issues were resolved
 - If cost rates changed, a determination is made to accept them
 - Contract provisions contain applicable fiscal provisions
- B. If a preaward audit was conducted by a local agency
 - Items in "A" above are satisfied

- Review work papers of preaward audit report and determine that the issues were resolved satisfactorily

OBJECTIVE

The purpose of a preaward audit is to provide professional advice on accounting and financial matters and to assist in the award and administration of proposed consultant contracts. A preaward audit also serves to alert both the consultant and the local agency of potential problems concerning the consultant's financial qualifications, basic contract, cost/price proposal or cost accounting system. The preaward audit examines the consultant's accounting, estimating, and administrative systems—as well as proposed costs, quantities, and financial condition.

The audit is as broad in scope as necessary to meet the following objectives:

- Determine if the consultant agreement specifically provides for the following:
 - Three year record retention period and right to audit
 - Method of payment
 - Reference to cost principles set forth in 48 CFR Chapter 1, Part 31 for allowability of individual items of cost; 49 CFR, Part 18 for administrative procedures; and OMB Circular A-110, which are administrative procedures for nonprofit subrecipients
- Determine if the Consultant's cost proposal contains a breakdown of the estimate for performing the work, and that the proposed costs are reasonable in relation to actual historical costs and estimating procedures
- Determine if the Consultant's cost accounting system is capable of accumulating reasonable, allocable, and allowable costs

PROCEDURE

Procedures to perform the preaward audit will depend on who the local agency elects to perform the audit.

Caltrans Performs Preaward Audit

For situations where a local agency elects Caltrans to perform the audit, the local agency must transmit a preaward audit request (see Exhibit 10-A) to the District Local Assistance Engineer (DLAE) with copies of the proposed consultant contract and cost proposal. The agency needs to advise the consultant that an audit needs to be performed and that cooperation with the auditors is expected. The DLAE, through the headquarters Office of Local Programs area

engineer, requests the audit by Caltrans' Audit and Investigations. Five weeks should be allowed for the average audit.

Local Agency (or hired CPA) Performs Preaward Audit

If the local agency performs the preaward audit, Exhibit 10-J must be transmitted to the DLAE prior to entering into a contract with a consultant(s). This is usually accomplished when the local agency submits the request for authorization to proceed with preliminary engineering (Exhibit 3-A for Federal-aid projects). The audit must be completed before the consultant contract is executed. Failure to do this will result in loss of funds for the consultant services. The audit must be performed in accordance with generally accepted government auditing standards promulgated by the United States General Accounting Office.

The local agency shall follow the attached brochure entitled *Audit and Accounting Guidelines for Negotiated Contracts with Caltrans* to assure that the audit objectives are clear as to the basic elements of an accounting system. In addition, the attached *Standard Audit Program Procedures* shall be used as the minimum procedures to be performed for the preaward audit.

The local agency shall submit preaward audit procedures to Caltrans Audits and Investigations prior to conducting a preaward. Such procedures need only be sent one time unless requested by Caltrans. Caltrans Audits and Investigations may perform a review of such procedures and express an opinion on them as needed.

Caltrans shall retain the right to audit or review the work of the local agency or designee at any time.

Preaward Audit not Performed

If a preaward audit was conducted on the consultant within the last 12 months, the local agency (or hired CPA) does not have to conduct the preaward audit if a copy of the previous preaward audit is reviewed, cited issues were resolved, any cost rates changed—it was determined to be acceptable, contract provisions contain applicable fiscal provisions, and a review of the preaward audit work papers were found to have issues that were resolved satisfactorily. Exhibit 10-J shall be completed for this situation.

Negotiation may begin with the consultant while the audit is being prepared.

Discussion should focus on technical aspects of the work and any discussion of costs should be limited until the audit results are received. The contract shall not be executed until the audit report has been completed and the consultant's accounting system, rates charged, knowledge of FHWA's cost eligibility, and documentation requirements are found satisfactory by the auditors.

Exhibit 3-A, "Request for Authorization to Proceed with Preliminary Engineering," includes boxes that indicate compliance with the preaward audit requirement when there is Federal-aid participation.

Exhibit 10-A is a sample request for a preaward audit to be performed by Caltrans. Sections 3.5.5 and 3.5.6 of the Caltrans' *Consultant Services A&E Manual* provide additional details about the audit process.

Exhibit 10-J must be signed by the local agency financial officer and by the DLAE to acknowledge receipt of the Audit Disposition and to establish the date when reimbursement of the consultant contract can be requested.

A courtesy copy of preaward audits conducted by the local agency shall be mailed to Caltrans' Office of Audits and Investigations, P.O. Box 942874, Sacramento, CA 94274-0001. This is for the purpose of maintaining a database of audited consultants, of which information is available by request.

The local agency is responsible for complying with these preaward audit procedures. In the event it is found by Caltrans or FHWA (or FTA) that the reimbursed consultant costs resulting from a lack of contract provisions, unallowable or unsupported activities, or an inadequate accounting system are the responsibility of the local agency—the local agency will be subject to the sanctions mentioned in Chapter 20 of this manual.

This new procedure will be included in the next manual change as well as on the Local Programs Home Page on the Internet at www.dot.ca.gov/hq/LocalPrograms.

Attachments

**REQUEST FOR AUTHORIZATION
TO PROCEED WITH PRELIMINARY ENGINEERING (PE)***Local Agency Letterhead*

To: (DLAE Name)
District Local Assistance Engineer
Caltrans, Office of Local Assistance
(District Address)

Date: _____
(Federal Number)
(Project Description)

Dear (DLAE Name):

In order to begin reimbursable preliminary engineering for the above project, we request that you secure Federal authorization and obligate funds for this work. The amounts requested do not exceed the Federal funds provided to this agency in the approved Federal TIP/Federal Statewide TIP (FSTIP).

Attached are the following documents that are required to authorize this phase of work:

Request for Authorization Package

- ☐ Completed Project Prefix Checklist (Exhibit 3-E)
- ☐ Completed Finance Letter (Exhibit 3-F)
- ☐ Completed Data Sheets (Exhibit 3-G)

Field Review Form (Exhibit 7-B)

- ☐ Completed Field Review form, or
- ☐ I will not be preparing the final design at this time. I will transmit the Field Review Form at a later date.

Environmental Document

- ☐ Approved Environmental Document
Type of Document _____
Approval Date _____
- ☐ I have not completed the environmental process and will not be preparing the final design at this time. I will transmit the Environmental Document at a later date.

Pre-Award Audit

- ☐ Completed Audit Disposition (Exhibit 10-J), or
- ☐ Audit Disposition was not completed because Federal-aid highway funding will not participate in a consultant contract, or
- ☐ Preaward audit was not done because the consultant contract is for \$75,000 or less, or
- ☐ I will not submit the Audit Disposition at this time. I will submit it to the DLAE prior to entering into a contract with the consultant(s).

I understand that invoice requests for payment will not be processed until a Program Supplement Agreement and Federal-aid Project Agreement (PR-2) have been executed.

(Check which of the following applies)

- ☐ I plan to request early reimbursement and invoicing for PE costs as incurred. As indicated above, I have included a completed Field Review Form. I am also including the "Agreements Checklist" (Exhibit 4-A) request forms with this transmittal and request that the agreements be prepared now.
- ☐ I do not plan to invoice for PE costs until this phase of the work is completed. I will transmit the "Agreements Checklist" at a later date.

I will not submit any invoice request until I receive notification that the Program Supplement Agreement and PR-2 have been executed.

CERTIFICATION

I certify that the facts and statements in this "Request for Authorization Package" are accurate and correct. This Agency agrees to comply with the applicable terms and conditions set forth in Title 23, U.S. Code, Highways, and the policies and procedures promulgated by the Federal Highway Administrator and the California Department of Transportation relative to the above designated project.

I understand that each succeeding phase of the project will require a separate authorization to be eligible for Federal reimbursement. I further understand that this Agency is responsible for costs in excess of the Federal funds obligated and all costs incurred before it has received FHWA "Authorization to Proceed" for that phase of the project.

Please advise us as soon as the authorization has been received. You may direct any questions to (Name _____) at (phone number _____).

Signed _____
Title _____
Agency _____

Attachments

EXAMPLE

PRE-AWARD AUDIT REQUEST LETTER

Local Agency Letterhead

To: (DLAE Name)
District Local Assistance Engineer
Caltrans, Office of Local Assistance
(District Address)

Date: _____
(Federal Number)
(Project Description)

Dear (DLAE Name):

Attached is a copy of (Agency Name) proposed contract number _____ with (Consultant's Name). Please arrange a pre-award evaluation and forward a copy of the written report to us. Services to be performed under this contract are (describe work to be performed).

Choose one:

(Agency Name) submitted a "Request for Authorization" for this work and the "Authorization to Proceed" was approved on (Date).

(Agency Name) will submit a "Request for Authorization" for this work prior to award of the consultant contract. The agency understands that any work prior to the approval of the "Authorization to Proceed" is not eligible for Federal fund reimbursement.

Please notify us of the estimated completion date of the audit.

If you need further information, please contact (Name) at (Phone #).

Sincerely,

Signed _____
Title _____
Agency _____

Attachments: Proposed Contract Language
Initial Cost Proposal

EXAMPLE

PRE-AWARD AUDIT REQUEST DISTRICT MEMO

To: Office of Local Programs
Attn: Area Engineer
1120 N Street, MS 1
Sacramento, CA 95814

Date: _____
(Federal Number)
(Project Description)

From: (DLAE Name)
District Local Assistance Engineer
Caltrans, Office of Local Assistance
(District Address)

Subject: Pre-Award Audit

Attached is a copy of (Agency Name) request for audit and proposed contract for contract number _____ with (Consultant's Name). Services to be performed under this contract are (describe work to be performed). Please arrange a pre-award evaluation by Caltrans Audits and Investigations and have them forward a copy of the written report to us and directly to the agency.

Please have OEA complete the lower portion of this memo and return it to this office to verify receipt and allow us to notify the agency of the estimated audit completion date.

Attachments: Agency Letter
Proposed Contract Language
Initial Cost Proposal

DATE _____

VERIFICATION OF PRE-AWARD EVALUATION REQUEST

Agency _____
Contractor _____
Contract Number: _____ Audit P# _____
Date Received by Audits Office _____
Auditor Assigned _____ Phone _____
Estimated Completion Date _____

AUDIT DISPOSITION

Date: _____

Agency Name: _____

Federal Number: _____

The following information documents the disposition of the required preaward (prenegotiation) audit prescribed in 23 CFR 172.5 (c). This form shall be completed for each consultant contract greater than \$75,000 with participating State or Federal-aid highway funds.

Check appropriate box:

Caltrans Performs Preaward Audit or Determines it is not Necessary

- ☐ Caltrans' Audits and Investigations performed the preaward audit and found the consultant satisfactory.
- ☐ For projects less than \$250,000, Caltrans' Audits and Investigations did not perform the preaward audit because a previous preaward audit (within the last 12 months) was obtained, cited issues were resolved, any cost rate changes were found acceptable, and contract provisions contain applicable fiscal provisions.

Local Agency (or hired CPA) Performs Preaward Audit or Determines it is not Necessary

- ☐ Preaward audit completed. Consultant found satisfactory.
- ☐ For projects less than \$250,000, a preaward audit was not done because a previous preaward audit (within the last 12 months) was obtained, cited issues were resolved, any cost rate changes were found acceptable, contract provisions contain applicable fiscal provisions, and a review of the work papers of the previous preaward audit were found to have issues that were resolved satisfactorily.

Signature of local agency financial/auditing officer

Title _____

I acknowledge receipt of this form and, to the best of my knowledge, believe the information contained is correct.

District Local Assistance Engineer _____ Date _____

Distribution: 1) DLAE
2) Project Files

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Standard Audit Program Procedures

Preaward Audit
(Name of Contractor)
Sample - Audit Program

W/P No:
Audit No:
Contract No:
Auditor:
Reviewer:

ITEM NO.	Audit Program Contents	AUDITOR INIT/DATE
I	<p>Purpose</p> <p>The purpose of a preaward evaluation is to provide the approving authority with professional advice on accounting and financial matters and to assist in the award and administration of proposed consultant contracts. It also alerts both the consultant and the approving authority to potential problems relative to the Consultant's basic agreement, cost/price proposal, procurement procedures, or cost accounting system.</p>	
II	<p>SCOPE</p> <p>The examination shall include reviews of applicable laws and regulations, the contract requirements, and the Contractor's system of internal controls. Audit tests of accounting records and such other auditing procedures considered necessary to meet the objectives will be conducted. Applications of audit procedures will be governed by the individual contract under audit.</p>	
III	<p>STANDARDS</p> <p>The audit is to be conducted in accordance with generally accepted governmental auditing standards.</p>	
IV	<p>APPLICABLE RULES AND REGULATIONS</p> <ol style="list-style-type: none"> 1. Contract Provisions 2. CFR 48, Part 31- Federal Cost Eligibility 3. CFR 49, Part 18- Uniform Administrative Requirements 	
V	<p>OBJECTIVES</p> <ol style="list-style-type: none"> 1. To determine if the consultant agreement specifically provides for the following: <ul style="list-style-type: none"> o three-year record retention period and right to audit. o method of payment o references to cost principles set forth in CFR 48, Chapter 1, Part 31 for allowability of individual items of cost; CFR 49, Part 18, for administrative procedures; and OMB Circular A-110, for nonprofit subrecipients. 2. To determine if the Consultant's cost proposal contains a breakdown of the estimate for performing the work, and that the proposed costs are reasonable in relation to actual historic costs and estimating procedures. 3. To determine if the Consultant's cost accounting system is capable of accumulating reasonable, allocable, and allowable costs. 	
VI	<p>PRELIMINARY AUDIT STEPS</p> <ol style="list-style-type: none"> 1. Review the proposed contract. <ol style="list-style-type: none"> a. Document your review and note any exceptions needed to be included on the audit report. 	

Standard Audit Program Procedures

Preaward Audit
(Name of Contractor)
Sample - Audit Program

W/P No:
Audit No:
Contract No:
Auditor:
Reviewer:

ITEM NO.	Audit Program Contents	AUDITOR INIT/DATE
	<p>2. Review the permanent file.</p> <p style="padding-left: 20px;">a. Ascertain the nature, timing, and extent of the last internal control and accounting system review.</p> <p>3. Review the cost proposal.</p> <p style="padding-left: 20px;">a. Determine if the Consultant's cost/price proposal contains a breakdown of the estimate for performing the work.</p> <p style="padding-left: 20px;">b. Foot and extend cost data.</p> <p style="padding-left: 20px;">c. Obtain missing cost proposal information, if necessary.</p> <p style="padding-left: 20px;">d. Compare data with permanent file. Obtain updated cost information, if necessary.</p> <p style="padding-left: 20px;">e. Comment on unusual amounts, unfavorable trends or differences between current and past costs.</p> <p style="padding-left: 20px;">f. Recalculate cost proposal in consideration of any audit exceptions.</p> <p>4. Determine scope of audit.</p> <p style="padding-left: 20px;">a. Omit audit step 2 (field work) if:</p> <p style="padding-left: 40px;">- a recent audit found the accounting system adequate, and</p> <p style="padding-left: 40px;">- the accounting system is adequate to accumulate and segregate additional contract costs.</p> <p style="padding-left: 20px;">b. If the accounting system has not recently been reviewed or does not appear to be able to take on additional contract costs, discuss the nature, timing, and extent of audit procedures with supervisor.</p> <p>5. Prepare preliminary Audit Plan and Time Budget</p> <p>6. Contact the Contract Administrator to inform him/her of the following:</p> <p style="padding-left: 20px;">a. Scheduled date of field work.</p> <p style="padding-left: 20px;">b. Tentative completion date.</p> <p style="padding-left: 20px;">c. Any anticipated problems, etc.</p> <p>Note: The Contract Administrator should be kept abreast of all pertinent audit issues. Any problems in obtaining necessary information, etc., should be discussed with him/her immediately and documented in the work papers.</p>	
VII	<p>AUDIT STEPS - FIELD WORK</p> <p>1. Contact the Contractor and arrange a date for the audit.</p> <p style="padding-left: 20px;">a. Inform the Contractor of the type of information, records, and personnel needed, and arrange for work space.</p>	

Standard Audit Program Procedures

Preaward Audit
(Name of Contractor)
Sample - Audit Program

W/P No:
Audit No:
Contract No:
Auditor:
Reviewer:

ITEM NO.	Audit Program Contents	AUDITOR INIT/DATE
	<ul style="list-style-type: none"> b. Request that the Contractor prepare schedules of the calculations of all billing rates such as overhead, fringe benefits, in-house direct cost billing rates and any other rates used in billing. If possible, have these schedules sent to the auditor for review before the date of field work. c. Inquire whether the Contractor has been audited within the previous year by the DCAA or similar Federal agencies, or has had an independent CPA review overhead, internal controls or project costing systems. If so, obtain a copy of the audit report and/or review working papers for consideration when evaluating internal controls, overhead rates, etc. d. Prepare and send an engagement letter to the Contractor to confirm the above discussion. Send a copy of the letter to the Contract Administrator. <p>2. Conduct an entrance conference with the Consultant to ensure coverage of the following:</p> <ul style="list-style-type: none"> - Purpose, scope and objective of the preaward evaluation. - Anticipated time frame of audit field work. - Whether the Consultant is familiar with CFR 48, Chapter 1, Part 31. If not, Consultant can call (202) 783-3238 to obtain a copy of these regulations. - Records, etc. needed to perform the audit. - Intention to keep Consultant updated on audit progress and to discuss all audit exceptions prior to issuance of an audit report. - Documentation of the entrance conference in the work papers. 	
VIII	<p>Control Structure Survey</p> <p>1. Review and evaluate the Contractor's internal control structure.</p> <ul style="list-style-type: none"> a. Prepare or update a written narrative, flowchart and/or completed internal control questionnaire which adequately describes the accounting system including significant internal controls over contract costs in order to adequately plan the audit and test the various applications. This understanding should include knowledge of the Contractor's control environment, accounting system and control procedures. Generally, the relevant policies and procedures pertain to a Contractor's ability to record, process, summarize, and report contract and financial information and to ensure compliance with applicable laws and regulations. b. Selectively examine (test) the accounting records and underlying source documents only to the extent necessary to determine if the system has the ability to accumulate and segregate reasonable, allocable and allowable costs through the use of a cost accounting system. The following are some of the attributes which should ideally be found in such a system: 	

Standard Audit Program Procedures

Preaward Audit
(Name of Contractor)
Sample - Audit Program

W/P No:
Audit No:
Contract No:
Auditor:
Reviewer:

ITEM NO.	Audit Program Contents	AUDITOR INIT/DATE
	<p>Chart of accounts (direct and indirect accounts).</p> <ul style="list-style-type: none"> - Segregation of costs by contract, category of cost and milestones (if applicable). - Proper recording of direct and indirect costs. For example, separate accounts should be used for direct labor, indirect labor, vacation, holiday, sick leave, etc. - consistent accounting treatment of costs in recording and reporting. - Ability to trace from invoices billed to job cost records and original, approved source documents to the general ledger. 	
2.	Prepare a summary of the internal control structure and cost accounting system. The summary should include or reference to a control risk assessment. Finalize Audit Planning document	
3.	Evaluation of cost/price data.	
	<ul style="list-style-type: none"> a. Obtain source documents and/or other criteria used to establish the cost/price proposal. 	
4.	Evaluate the propriety of direct labor costs.	
	<ul style="list-style-type: none"> a. Select a representative sample of employee timesheets (cards) and test the hourly extensions. b. Trace hours to the payroll journal and compare hourly rates paid to the rates submitted with the cost/price proposal. c. If applicable, compare proposed direct labor rates to prevailing wage and union labor rates. d. If overtime is proposed, does the Consultant have procedures to ensure and document equitable overtime charges to government and non-government contracts? e. Prepare a labor rate analysis and comment on variances. 	
5.	Analyze indirect costs (fringe benefits, overhead, general and administrative).	
	<ul style="list-style-type: none"> a. Request written verification of an approved overhead rate, if available (DCAA or other qualified entity). b. Obtain a written breakdown/schedule of costs included in the rates. <ul style="list-style-type: none"> - Trace the indirect rate schedule to the general ledger. - Scan the indirect cost accounts in the general ledger for unallowable costs. 	

Standard Audit Program Procedures

Preaward Audit
(Name of Contractor)
Sample - Audit Program

W/P No:
Audit No:
Contract No:
Auditor:
Reviewer:

ITEM NO.	Audit Program Contents	AUDITOR INIT/DATE
	<ul style="list-style-type: none"> - Test the Consultant's proposed rate by comparing the individual items of cost for allowability and fair presentation with CFR 48, Ch 1, subpart 31.203. c. Schedule all disallowed costs. d. Recalculate the overhead rate and comment on variances. <p>6. Evaluate the propriety of other direct costs (materials, transportation, equipment, per diem, etc.) and Subcontractors.</p> <ul style="list-style-type: none"> a. Determine the methods used to establish the cost materials, transportation, and per diem, etc. b. Compare proposed rates or costs with prevailing rates or past experiences. c. Determine if direct costs are independent from the indirect cost pool. d. Schedule all costs which do not appear to meet the criteria established in CFR 48, Chapter 1, Subpart 31.2. <p>7. Evaluate the proposed fixed fee.</p> <p>As field work progresses, keep the Controller or other contact person aware of the findings or problems as they arise. Resolve the matters if possible. Document these conversations in the work papers.</p> <p>8. Evaluate the Contractor's financial capability - Ratio Analysis</p> <p>9. Prior to completion of field work, discuss all exceptions with the consultant ensuring coverage of:</p> <ul style="list-style-type: none"> - Scope and objectives of the preaward audit. - The condition, criteria, cause, effect, and recommendation for each exception noted. - Caltrans' review process and reporting procedures. - Any questions the Consultant may have. 	
IX	<p>COMPLETION</p> <ul style="list-style-type: none"> 1. Complete work papers to assure that they are properly headed, indexed, signed, dated, and cross referenced. In addition, each work paper should include, or be reference to, a statement of purpose, source, analysis and conclusion. 2. Prepare an audit summary which documents the purpose, objectives, procedures, results/conclusions and recommendations. 3. Cross reference all exceptions to the appropriate work papers. 4. Prepare draft audit report. 	

Standard Audit Program Procedures

Preaward Audit
(Name of Contractor)
Sample - Audit Program

W/P No:
Audit No:
Contract No:
Auditor:
Reviewer:

ITEM NO.	Audit Program Contents	AUDITOR INIT/DATE
	<p>5. If necessary, schedule a close out conference with the Consultant to discuss any exceptions not discussed or resolved as of completion of fieldwork. Also, if material findings are identified, the Contract Administrator should also be contacted. Document these conversation/conferences.</p> <p>6. Complete audit assignment card.</p> <p>7. Update the permanent file.</p> <p>8. Submit completed work papers and draft audit report to supervisor for final review.</p> <p>9. Prepare final report and distribute as follows:</p> <ul style="list-style-type: none"> * Original - Requester * If Requester is headquarters than: 1 copy - Headquarters Contract Office * If Requester is District than: 1 copy - District Contract Officer or District Consultant Services * 1 copy - Audit file (Section B) * 1 copy - Chronological File (Audit Reports Binder) * 1 copy - P# File (Audit Reports Binder) * 1 copy - Audit Office * 1 copy - Supervisor <p>NOTE: A "cc" notation is needed on the final report for reports distributed outside of the audits office.</p>	

Accounting

&

Auditing

**GUIDELINES FOR
CONTRACTS
WITH CALTRANS**





ACCOUNTING SYSTEM

Contractors (whether a prime or subcontractor) planning to contract with Caltrans must have an accounting system which meets the following objectives:

- The ability to record and report financial data in accordance with generally accepted accounting principles.
- A system of record keeping to ensure that costs billed to Caltrans are:
 - a. Supported by adequate documentation.
 - b. In compliance with the terms of the contract and applicable Federal and State regulations specified in the contract.
- A system of record keeping ideally includes the following:
 - a. General ledger
 - b. Job cost ledger
 - c. Labor distributions
 - d. Time records
 - e. Subsidiary journals
 - f. Chart of accounts
 - g. Financial statements
- The ability to accumulate and segregate reasonable, allocable (incurred solely for a project) and allowable (per terms of the contract) costs through the use of a cost accounting system. The following are some of the attributes which would ideally be found in such a system:
 - a. A chart of accounts which includes indirect and direct general ledger accounts. Indirect costs are not specifically identified to a project, for example, rent and/or utilities. Direct costs are specifically identified with a project, for example, drafting hours and/or design hours.
 - b. Segregation of costs by contract, category of cost and milestones (if applicable).
 - c. Proper recording of direct and indirect costs. For example, recording of labor costs should provide that non-project indirect hours be recorded on a time sheet and in the accounting records to an administration, vacation, sick leave or other indirect cost account/code. Direct project hours should be recorded on a time sheet and in the accounting records to a direct project cost account/code.

INTRODUCTION

The purpose of this brochure is to outline for you, a potential contractor with the California State Department of Transportation (Caltrans), the basic elements of an adequate accounting system, and the types and objectives of audits that will be performed in relation to your contract. In order to successfully compete for a contract and meet the audit requirements, a contractor (whether a prime or subcontractor) must have a system of record keeping and internal control. Although a specific cost accounting system is not required, a contractor needs a system which will assure compliance with the terms of the agreement. A preaward audit will be performed to assure you meet these requirements prior to contract execution. If your system is deficient, the contract will not be executed.

Caltrans reimburses, through your overhead rate, the costs attributable to establishing and maintaining a cost accounting system.

Staff time and other costs related to an audit performed of your contract are normally reimbursed through your overhead rate.

3
95
8
702
29
95
218
2

- d. Consistent accounting treatment of costs in recording and reporting. For example, if travel expense is charged directly to a project, all travel expense incurred on any project should be considered a direct cost. As a result, project-related travel, whether reimbursable per the contract terms or not, should be included as a direct cost.
 - e. Ability to trace from invoices submitted to Caltrans to job cost records and original, approved source documents, for example, time sheets, vendor invoices, cancelled checks.
 - f. Ability to reconcile job cost records to the accounting records.
- Compliance with cost principles described in the Code of Federal Regulations 48, Federal Acquisition Regulations System (FAR), Chapter 1, Part 31. Information on how to obtain this regulation is described under "Audit Criteria" on the following page.
 - Procedures to monitor and adjust projected overhead rates to actual rates.
 - Controls to ensure that written approval is obtained prior to any changes to the contract.
 - Procedures to retain accounting records and source documentation as required by the terms of the contract.
 - A system of internal control which provides reasonable assurance that assets are protected; financial data, records and statements are reliable; and errors and irregularities are promptly discovered, reported and corrected. The elements of a system of internal control should include, but not be limited to, the following:
 - a. Separation of duties for proper protection of assets. Incompatible duties are those that place any person in a position to both perpetrate and conceal errors or irregularities in the normal course of business. For example, the person who writes checks should be different from the person who reconciles bank statements and the person who purchases goods should be different from the person who receives goods.
 - b. Limiting access to assets to only authorized personnel who require these assets in the performance of their assigned duties. For example, blank check stock should be locked in a safe when not in use.
 - c. Authorization and record keeping procedures which provide effective accounting control over assets, liabilities, revenues, and expenditures.
 - d. A system of practices to be followed in the performance of duties and functions. Such a system normally includes policies and procedures which establish the purpose and requirements of the accounting system. For example, timekeeping practices should ideally provide for the following:
 - Time sheets be prepared, signed and dated by all employees.
 - Time sheets be completed in non-erasable ink.
 - Time sheet corrections be crossed out and initialed by the employee.
 - Time sheets be signed by a supervisor as reviewed and retained on file as required by the contract.
 - e. Personnel with skills and training commensurate with their responsibilities.
 - f. A system of internal review. For example, bank reconciliations and travel expense claims should be reviewed, approved, and signed by a supervisor.



AUDITS

Contractors, whether a prime or subcontractor, performing under a negotiated contract with Caltrans are subject to the following audits.

- **Preward Audits:** Prior to the award of a contract, Caltrans Audits and Investigations will conduct a preward audit to determine if the contractor's accounting system is adequate to accumulate and segregate costs as detailed in the previous section and to determine if the proposed costs are reasonable. The audit alerts both the contractor and Caltrans management to problems relative to the contractor's cost proposal and cost accounting system. Due to time constraints in the award process, your cooperation in scheduling the preward audit with short notice will expedite the execution of your contract.
- **Interim Audits:** Interim audits are performed on an as needed basis. During the preward audit, if it is determined that the contractor's accounting system is new or minor deficiencies are noted, an interim audit is scheduled to determine that the system is functioning adequately to ensure that billed costs are supported and that any deficiencies were corrected. An interim audit may be requested by the contract administrator or by Caltrans management to address concerns during the course of the contract. Also, an audit manager may initiate an interim audit of a multi-year contract to ensure that costs reimbursed to date are allowable.
- **Post Audits:** Post audits of contracts are performed routinely after project completion. Post audits are performed to determine whether the costs claimed are allowable, allocable, reasonable, and in compliance with the Federal and State laws and regulations as well as the fiscal provisions stipulated in the contract. The examination includes reviews of applicable laws and regulations, the contract requirements and the contractor's internal control system. Audit tests of the contractor's accounting records and other auditing procedures considered necessary will also be performed. Applications of all audit procedures would also be governed by the individual contract under audit. Unsupported or unallowable costs are normally the result of weaknesses in the accounting system and will be reimbursed to Caltrans.

To provide contractors with a procedure for obtaining prompt and equitable resolution to a dispute arising from a post audit of a non-highway construction cost reimbursement contract, Caltrans has established an Audit Review Committee (ARC). Information explaining the ARC should be found in your contract and/or as an attachment to the post audit report.

AUDIT CRITERIA

For specific information regarding basic cost accounting systems and applicable State and Federal regulations, please see the following:

- **Code of Federal Regulations 48, Federal Acquisition Regulations System, Chapter I, Part 31:** This regulation contains cost principles and procedures for the pricing of contracts/subcontracts and the determination, negotiation, or allowance of costs. Contact:

**Superintendent of Documents
Government Printing Office
Washington, DC 20402**

**Washington, D.C. (202) 512-1800
San Francisco (415) 512-2770
Los Angeles (213) 239-9844**

- **California State Administrative Manual:** A reference source for statewide policies, procedures, regulations and information. Contact:

**Office of State Publishing,
Department of General Services.
Call for order form: (916) 445-2295.**

For review of the above references, contact your local library or the California State Library.

**California State Library
Library and Courts Building
914 Capitol Mall, P.O. Box 942837
Sacramento, CA 94237-0001**

Information: (916) 654-0261

For assistance in establishing an accounting system which will meet the objectives outlined in this brochure, you should contact an accountant and/or bookkeeper who is familiar with cost accounting systems.